

Before The
POSTAL RATE COMMISSION
WASHINGTON, D.C. 20268-0001

Stamped Stationery Classification

)

Docket No. MC2006-7

INITIAL BRIEF

OF

THE OFFICE OF THE CONSUMER ADVOCATE

Shelley S. Dreifuss
Director
Office of the Consumer Advocate

Kenneth E. Richardson
Attorney

May 4, 2007

TABLE OF CONTENTS

<u>OFFICE OF THE CONSUMER ADVOCATE (OCA) POSITION</u>	3
<u>PROCEDURAL HISTORY</u>	3
<u>ARGUMENT</u>	5
A. Stamped Stationery	7
1. Costs of the Premium Stamped Stationery Product.....	8
2. Proposed Implicit Cost Coverages Are Excessive	9
3. The Postal Service's Price Ranges Are Unjustified.....	11
4. Cost Coverages Were Not Sufficiently Considered by Witness Yeh.....	14
5. The Pricing Factors in §3622 of the PRA Are Not Met.....	15
6. The Value of the Premium Stamped Stationery Does Not Warrant A High Cost Coverage.....	18
B. Premium Stamped Cards	21
<u>CONCLUSION</u>	26

Before The
POSTAL RATE COMMISSION
WASHINGTON, D.C. 20268-0001

Stamped Stationery Classification)

Docket No. MC2006-7

INITIAL BRIEF
OF
THE OFFICE OF THE CONSUMER ADVOCATE

OFFICE OF THE CONSUMER ADVOCATE (OCA) POSITION

The Office of the Consumer Advocate (“OCA”) hereby files its initial brief in this proceeding in support of the Postal Service’s proposed new permanent special services classifications for Premium Stamped Stationery (PSS) and Premium Stamped Cards (PSC). The OCA favors the Postal Service’s proposal to establish a range of rates for the Premium Postal Stationery and the Premium Post Card classifications. The novel application of a rate range will eliminate the burden of modifying rates either up or down within the range and provide management significant price flexibility in marketing these products.

However, OCA opposes the level of the proposed price ranges for two reasons. First, the Postal Service proposes tying the price ranges to a multiple of the First-Class letter rate and the card rate. Although this approach of using a range of prices was

suggested by the Commission in Order No. 1475 as possibility for consideration by the Postal Service,¹ in OCA's view, tying these products to a multiple of the First-Class single-piece letter and card rates would not be consistent with historical and current pricing policies of the PRC. The costs of production and distribution of these products is unrelated to the postage rate for letters or cards.

A second reason for OCA's objection to the Postal Service's proposed range of fees is that the proposed range of fees 2 to 3 times the First-Class letter rate for the Premium Stamped Stationery is unsupported by the cost evidence in this proceeding and is far in excess of a reasonable cost coverage, even if greater than normally applied cost coverages are allowed to account for the special value claimed to be inherent in these products. The implicit cost coverage of the stationery at current prices falls outside a reasonable level; and the selling price of the stationery should be reduced.

The Commission should recommend fees in the case of the Premium Stamped Stationery from \$0.302 to \$0.613 based on a range of cost coverages from 104.1 percent to 211.6 percent for the stamped enveloped and the highest cost coverage in Docket No. R2006-1. The range is also based on the average cost of the two Premium Stamped Stationery issues. To avoid unnecessary expense, the price should not be reduced until current stocks are sold or destroyed. The Premium Stamped Cards implicit cost coverage within the maximum proposed fee is also excessive. The range of PSC fees should be reduced to a level with cost coverages between that allowed for the utilitarian stamped cards and the highest cost coverage allowed in the last rate case, Docket No. R2006-1, for a fee range of \$0.189 per unit to \$0.296 per unit. The price of the PSCs currently on sale falls within this range.

¹ "Order Concerning Stamped Stationery," Docket No. C2004-3, August 24, 2006.

PROCEDURAL HISTORY

The genesis of this proceeding was a complaint filed June 24, 2004, by Mr. Carlson in Docket No. C2004-3, claiming stamped stationery is a postal service within the meaning of §§3621, 3622, and 3623 of Title 39 of the U.S. Code, as well as under the Commission's Rule No. 5(s).² Subsequently, the Commission determined stamped stationery is a postal service subject to the Commission's classification and rate jurisdiction.³ Upon reaching that conclusion, the Commission thereupon initiated this proceeding to provide the Postal Service the opportunity to file a classification and rate request for stamped stationery, if it so chose, or to defer from filing a request, in which case the Commission would issue a further order in the proceeding.⁴

The Postal Service filed its request in this docket on February 22, 2007. With its Request, the Postal Service filed the prepared testimony of witness Yeh including 2 workpapers in Attachment A to the testimony. No party requested a hearing, and efforts to reach settlement among the parties were unsuccessful. The final date for interrogatories was April 19, 2007. Initial briefs are due May 4, 2007, and reply briefs are due to be filed May 14, 2007.

The Postal Service not only requests a new SpecialServiceclassification and rate for Premium Stamped Stationery (Proposed Fee Schedule 963 and DMM §963), the subject of the earlier docket, but also requests a new Special Service classification and rate for Premium Stamped Cards. (Proposed Fee Schedule 964 and DMM §964.)

² 39 C.F.R §3001.5(s).

³ PRC Order No. 1475, August 24, 2006.

⁴ PRC Order No. 1476, August 24, 2006.

The Postal Service indicates that although the Commission's order initiating this proceeding and the prior underlying complaint leading to this proceeding did not discuss stamped cards, the Postal Service acknowledges the similarity of the card product to the envelope product in terms of the application of the definition of a postal service to these products. Postal Service witness Yeh notes that "the same logic by which stamped stationery was deemed to be a 'postal service' applies to the stamped cards." (Yeh at 3). The Postal Service therefore requests a separate Special Service classification for Premium Stamped Cards.

According to the Postal Service, from the inception date of the PSS and PSC programs, their revenues have not exceeded \$2,700,000. (OCA/USPS-T1-13, DBP/USPS-1.)⁵ Only two formats of Premium Stamped Stationery have been sold: the Disney Friendship stationery since January 2004 and the Garden Bouquet stationery since March 2005. (DBP/USPS-2.) No new stationery issues are currently planned. (DBP/USPS-1-7.) Combined, a total of 28,027 packages of 12 sheets of stationery have been sold at \$14.95. (DBP/USPS-1.)⁶

Several issues of Premium Stamped Cards have been sold dating back to 1994, of which only 10 are still on sale. (Ibid., DBP/USPS-20.) A new Premium Stamped Card is planned in late May, 2007. (DBP/USPS-1-7.) Stamped Cards containing designs or images were not sold at the price of the utilitarian stamped card, currently 2 cents (prices were first established in Docket No. R97-1), but at substantially higher prices.

⁵ For a table of the premium cards and premium stationery, the number sold, price, and total revenue, and non-postage revenue and other information, see DBP/USPS-35. Specific costs relating to each product are not available. (DBP/USPS-35(b).)

⁶ For a full list of the number of packages of stationery and cards printed and sold as of the end of March 2007, see DBP/USPS-52.

(See DBP/USPS-2.) The current Premium Stamped Card program is distinguished from the earlier cards sold between 1989 and 1993 where the printed stamp related to the theme of the card. The Premium Stamped Cards, which are the subject of this proceeding, feature designs from stamps issued specially for the cards. (Ibid., DBP/USPS-26.)

ARGUMENT

The issue in this proceeding is straightforward: what is the appropriate price or price range for these classifications. More specifically, whether (1) the record supports a Commission recommendation to diverge from precedent and recommend fees based on a benchmark of the First-Class rates which has no nexus to the costs involved, and (2) whether the cost coverages of the fees proposed are excessive and must be reduced to levels consistent with those allowed in recent omnibus rate cases.

OCA does not oppose Special Service classifications for the premium stamped stationery and stamped cards as proposed. The Request, together with the testimony of witness Yeh and the responses to the interrogatories, demonstrate these classifications are distinct from the current Special Service classifications for stamped envelopes and stamped cards. Witness Yeh summarized the statutory criteria within §3623 of the PRA in support of her classification recommendations. Witness Yeh explained that the changes in the classification schedule are in accordance with the factors set forth in §3623 of the PRA. (Yeh at 6-8.) As noted above, the OCA supports establishing new classifications for these two premium stationery products and believes they are consistent with the factors set out in §3623 of the PRA. (Yeh at 6-11.)

The Premium Stamped Stationery consists of “quality stock paper” featuring a design and imprinted with matching postage. (Yeh at 2.) The issues are denoted as premium to distinguish them from the more utilitarian stamped envelope. (Yeh at 3.) Moreover, the Premium Stamped Stationery is very different from current utilitarian stamped envelopes which are sold as a finished enclosed envelope but have no space for writing a message.

OCA does not take issue with the form of the products, their format, or the size of the packs in which they may be sold. Currently, the stationery is sold in packs of 12 and the cards are sold in packs of 20. The pricing mechanism proposed is to be based on a per unit price, thereby leaving the Postal Service the flexibility to package the products in the numbers it chooses. The Postal Service states it will give notice of any changes within the price range established (Yeh at 4), although the Postal Service wishes to avoid amending the DMCS and fee schedules for each PSS or PSC issuance. (OCA/USPS-T1-17.)

At the pre-hearing conference, the Postal Service was asked whether it had considered printing a “Forever” stamp on these products. (Tr. 1/5.) Interrogatory responses indicate the Postal Service does not have a basis to estimate whether there would be a net savings to the Postal Service if it imprinted a Forever Stamp on the stationery. (OCA/USPS-T1-32.) Nor does the Postal Service know whether it would be more cost effective to imprint a Forever Stamp rather than adding make-up stamps or destroying unsold packages at the time of rate increases. (OCA/USPS-T1- 34.) The Postal Service wishes to defer consideration of a Forever Stamp on the premium

stationery and cards pending establishment of the classifications and more experience with the actual Forever Stamp. (DBP/USPS-40.)

In the past, the Postal Service added make-up stamps to the Disney stationery packages, but not to the Garden Bouquet packages. The Postal Service has indicated the cost of adding make-up stamps to the package is not part of the production cost, but is a stamp fulfillment office cost, a cost not included in the attributable cost of the product. (DFC/USPS-T1-11, OCA/USPS-T1-30.) In the future, the Postal Service says make-up stamps will not be added to packages and the stationery will remain on sale with the old postage rate until sold. (OCA/USPS-T1-31.)

A. Stamped Stationery

OCA opposes the range of rates proposed for each of the premium stationery and card products. Fees approved in the most recent rate proceeding in Docket No. R2006-1 for the conventional stamped envelope and card products are in Fee Schedules 961 and 962, respectively. The fees for those utilitarian products are \$0.09 for a basic plain stamped envelope and \$0.02 for a single stamped card plus the value of postage. (PRC Op., Appendix One, at 110-111.) Those fees are derived from the attributable cost plus a reasonable amount for institutional costs. The Commission Opinion, in the last rate case in Docket No. R2006-1, recommended, and the Governors accepted, a stamped letter cost coverage of only 104.1 percent “because the service encourages the use of the mailstream....” (PRC Op. at 463-4.) To encourage the use of the mails the Commission favored a lower cost coverage.

1. Costs of the Premium Stamped Stationery Product

Postal Service witness Yeh provided production and distribution costs for the Garden Bouquet stamped stationery. The total cost per sheet is \$0.36, excluding postage, plus distribution and window service costs. The \$0.36 cost covers printing, packaging and shipping of the completed packs. (Yeh, Attachment A, PSSPSC-WP4.) To this, the witness used proxies to add distribution unit costs varying between \$0.00135 and \$0.00207. (Yeh at 6, DFC/USPS-T1-2..) In addition, witness Yeh added window service costs ranging from \$0.0002 to \$0.0515. (Ibid.) The range of proxies for the unit distribution cost and mail processing costs and window service selling unit costs were taken from the costs for Stamped Envelopes, in the record of Docket No. R2006-1. The proxies were added to the production costs to estimate a range of cost coverage for both the Premium Stamped Stationery and the Premium Stamped Cards. (DFC/USPS-T1-2, DFC/USPS-T1-10.)

The approximate costs for the Disney Friendship Premium Stamped Stationery were also provided. (OCA/USPS-T1-21, DFC/USPS-T1-8.) Production costs of \$0.22 were significantly lower than for the Garden Bouquet stationery. (OCA/USPS-T1-21) The distribution and window service costs noted above would be added to find total costs for that issue. Thus, combined, the average cost of the two issues, \$0.36 and \$0.22, is \$0.29.

The witness testified that complete cost estimates are not available because the costs are different for different issuances and have not been tracked. The production costs in the record are in the form of invoices from the printers for each of the two Premium Stamped Stationery products. (Yeh, Attachment B; OCA/USPS-T1-22.) There

were no additional expense payments outside the direct costs for printing and packaging. (DBP/USPS-7.) The Postal Service does not incur any additional costs for royalties for the use the images on the stationery and no other such fees have been paid. (DBP/USPS-70.) Although the witness suggests that the exact costs are unknown, the witness has not alluded to any other costs that are not included in the cost coverage calculations. Indeed, the costs may be overstated to the extent the proxies for window service or distribution are included. Much of the product is sold through the stamp fulfillment center where window service costs are not deemed attributable costs for any classes of mail or service. All of the selling costs of the stamp fulfillment center are treated as institutional costs. (DFC/USPS-T1-11.)

2. Proposed Implicit Cost Coverages Are Excessive

The cost coverages implicit in the range of rates proposed for the Premium Stamped Stationery of 2 to 3 times the First-Class letter rate are far in excess of the 104.1 percent cost coverage recommended for the stamped letter class in Docket No. R2006-1, and, for that matter, higher than the cost coverages recommended for any other Postal Service class of service.

The Postal Service proposes a maximum fee of three times the \$0.41 First-Class letter rate or \$1.23, excluding postage. For the Garden Bouquet premium stationery with approximated unit costs of 36 cents, this would yield the unacceptably high cost coverage of 342 percent. (OCA/USPS-T1-20(c).) Currently, the Garden Bouquet stationery is sold for \$14.95 for a package of 12 letter sheets. (OCA/USPS-T1-3.)⁷

⁷ The price has never changed. A different price posted on the website at one time was in error. (DBP/USPS-3.)

Even at the current price, the per unit price, excluding postage, of \$0.8558 provides a cost coverage for the Garden Bouquet of 238 percent. (OGC/USPS-T1-20.) This coverage is out of line with normal cost coverages for any and all postal products and particularly stamped envelopes.⁸ Even at the proposed minimum fee of 2 times the First-Class letter rate, or \$0.82, the cost coverage for the Garden Bouquet stationery would be 228 percent, also higher than any cost coverage recommended by the Commission in Docket No. R2006-1.

The Disney Friendship stationery sheets were less expensive to produce (DFC/USPS-T1-17), with approximate unit costs of 22 cents. The effective cost coverage at the maximum proposed fee of 3 times the First-Class rate, similarly calculated, is an eye-popping 559 percent cost coverage. (OCA/USPS-T1-21(c).) Even the cost coverage for the Disney sheets at the current price of \$0.8558 per sheet, excluding postage is inordinately high at 389 percent. (OCA/USPS-T1-21(b).)

If the costs of the two stationery products are averaged together (36 cents and 22 cents), the average cost is 29 cents. This avoids the de-averaging approach used by witness Yeh in order to determine the total costs for this class and the overall cost coverage. Based on the current price of \$0.8558 per sheet, the cost coverage at the current price is 295 percent ($\$0.8558/\0.29). At the maximum price proposed, three times the First-Class letter rate, the cost coverage would be an even more unacceptable

⁸ Even if the Premium Stamped Stationery were sold at the minimum rate in the range proposed of two times the First-Class rate, or \$0.92, the cost coverages of 256 percent for Garden Bouquet (92/36) and 418 percent for Disney Friendship (92/22) would be far in excess of the usual range. Moreover, even if the product were priced at, for instance, one times the rate for the First-Class letter rate, which might lower the cost coverage to an acceptable area, the OCA would still be opposed to the benchmark because there is no nexus between the price of First-Class letter rate and the cost of the Premium Stamped Stationery.

424 percent (\$1.23/\$0.29)⁹ These cost coverages at both the current selling price and the proposed maximum price, as well as the lack of nexus between the costs of the stationery and the First-class letter rate, clearly indicate that a benchmark other than the First-Class rate is needed to establish a reasonable maximum range for PSS fees.

3. The Postal Service's Price Ranges Are Unjustified

Witness Yeh attempts to justify the proposed price range at two to three times the First-Class letter rate for these products by starting, not with costs, but by comparing the price of the Premium Stamped Stationery letter sheet with the market price of stationery available commercially and in her own collection. (Yeh at 5 and Yeh, Attachment A, PSPSC-WP3.)¹⁰ It must be remembered that this study was not the basis for the current pricing of these products. The PSS are being sold at the price of \$0.8558 since 2004. (DBP/USPS-1.) The selling price was established by the Postal Service on the basis of comparable products and expected demand since the inception of the service, prior to the date the Commission ruled the service is a postal service. (OCA/USPS-T1-23.)

In witness Yeh's view, a price range based upon a markup of costs is not more appropriate than a price range based on a multiple of First-Class rates. (OCA/USPS-T1-24.) Her choice of the sales price range is not based upon a sophisticated demand study but apparently upon casual marketing decisions. The Postal Service is unaware of any studies that reveal the price elasticity of demand for either the stationery or the

⁹ Witness Yeh originally provided only the higher production costs for the Garden Bouquet stationery in her testimony on the theory that it is more recent than the Art of Disney Friendship production costs. (DFC/USPS-T1-16.) There are also significant differences in quality between the two products, causing higher production costs for the Garden Bouquet PSS. (DFC/USPS-T1-17.)

¹⁰ See also DBP/USPS-36 for greater details about the samples in the study. For confidence intervals of the study, see DBP/USPS-67.

cards. (DBP/USPS-30.) Without elasticity studies it is not known whether a lower price range tied more appropriately to reasonable cost coverages may actually increase demand and consequently overall revenue from these products. The Postal Service admits it has no studies that could refute this possibility.

Witness Yeh conducted an *ad hoc* study of “market prices of commercially available products that might serve as substitutes for the stationery.” (Yeh at 5.) The study includes samples of various qualities, size and features such as fold-and-mail attributes. (See OCA/USPS-T1-1, DBP/USPS-36.) Some letter sheets were of much lower quality than the quality of the PSS. (DBP/USPS-36(e).) The witness *assumed* the “full retail price.” She determined an average unit price per sheet of stationery, without postage, of \$1.115, based on various sample unit prices from \$0.22 to \$2.95. (OCA/USPS-T1-1.)¹¹ Witness Yeh “obtained and examined a sample of such products and used them to calculate the price points” proposed in this docket of two to three times the First-Class letter rate. (Yeh at 5). She did not use the traditional method of applying a markup to unit costs. (OCA/USPS-T1-23.)

After determining the rate, witness Yeh merely calculated the magnitude of the cost coverage to assure that approximated costs were covered.¹² Witness Yeh then demonstrated that the selling price is more than the attributable cost of the stationery products. Witness Yeh compared the total unit costs of the premium stamped stationery to the minimum rate proposed and concluded that the total unit cost would fall “well

¹¹ The fold-and-mail stationery items in the survey sold in pads of 40 sheets were only 22 cents per unit, far less expensive than any other items in the survey. (See DBP/USPS-36 (b-c), (f).)

¹² Witness Yeh uses the term “approximated” total unit cost rather than “attributable,” but she has not indicated any costs other than the production, distribution and proxy costs she has identified that might also be included to determine attributable costs. (OCA/USPS-T1-25, see also DBP/USPS-7.)

under” the minimum fee in the proposed range. (Yeh at 6.)¹³ She did not consider whether the cost coverages were excessive. (DFC/USPS-T1-30.)

In OCA’s view the cost coverages at the proposed fees are excessive. For instance, in Docket No. R2006-1, the cost coverage recommended for all mail and special services was 179.3 percent. (PRC Op., Vol. 2, App. G, at 50 (Sch. 3, Table 1).) The highest cost coverage recommended by the Commission for any subclass was 211.6 percent for First-Class letters. (Ibid.)¹⁴ In the omnibus rate cases ever since and including Docket No. R2000-1, except for the aberration for mailgrams, the highest cost coverage was 237.8 percent for the ECR and NECR Standard Mail subclass. In those cases, the Commission recommended a cost coverage exceeding 200 percent in only five instances. In earlier rate cases, including the Docket No. R90-1 rate case, the Commission recommended a cost coverage higher than 200 percent only three times. Except for an aberration for a high mailgram cost coverage, the other two coverages over 200 percent were for the Standard Mail ECR subclass at 203 percent in Docket No. R97-1 and 209.4 percent in Docket No. R94-1 (Ibid.). It is apparent that the implicit coverages for the price ranges proposed by the Postal Service are not close to traditional norms but are multiples of cost coverages historically recommended.

¹³ Witness Yeh’s initial testimony calculated the cost coverage for PSS would be between 215 to 216 percent, even at the minimum fee proposed—a price the Postal Service has not indicated it is likely to charge for these products and is well below the current price it is charging. Moreover, due to an adjustment in the calculations pursuant to interrogatories, the cost per unit are actually slightly lower than indicated in the prepared testimony, thus slightly increasing the cost coverage calculated in her original testimony. (See OCA/USPS-T1-20 and 21.)

¹⁴ The table referenced is a comparison of markups for all of the omnibus rate cases before the PRC beginning with Docket No. R71-1. The cost coverages are easily derived by adding 100 percent to each of the markups listed.

4. Cost Coverages Were Not Sufficiently Considered by Witness Yeh

Witness Yeh's responses to interrogatories demonstrate the limitations of her recommendations. Witness Yeh admitted that the cost of these stationery products was not a factor in her pricing recommendation. (OCA/USPS-T1-23.) Therefore, cost coverage was not relevant to the Postal Service's recommended pricing formula. On the other hand, the Commission's precedent provides no basis for diverging from costs as a basis for establishing the appropriate fee for this classification. The Commission's order, on which the Postal Service places so much weight in support of its novel approach to establish a range of prices for the product, did not condone or suggest that costs would not be important in setting the fee.¹⁵ The novel approach the Commission suggested was not that the Postal Service should set the price without regard to costs or cost coverages; rather, the novelty suggested was "novel pricing approaches." OCA does not oppose establishing a range of rates to afford the Postal Service some flexibility in pricing these products or similar products that, in all likelihood, will have different production costs. But that range should be tied to costs and a range of fees that effectively yield a cost coverage consistent with Commission precedents established under the PRA.

The Postal Service's justifications for the extreme cost coverages for these products rest on one primary argument: the products are a "premium" product which should command premium prices. First, it must be remembered that this is a product that is subject to the Postal Service's monopoly and is priced pursuant to the terms of

¹⁵

Docket No. C2004-3, Order No. 1475, August 24, 2006 at 13.

the Postal Reorganization Act. The Postal Service has not and cannot contend the terms of the PRA do not apply to this product.

The PRA provides in §3622(b)(3) that fees for each class must bear the attributable costs of the class plus a portion of all other costs reasonably assignable to such class. The Commission has time and again applied this standard carefully and rigorously when recommending prices. This new class is no different. Nor has the Postal Service demonstrated or even argued that this Premium Stamped Stationery class is somehow exempt from this section of the PRA. Yet, that is how the Postal Service witness has approached the pricing recommendations in this docket. Although minimal attention is paid to stating the assignment of institutional costs is reasonable, the Postal Service's case does not support that conclusion. In fact, the witness has clearly admitted that the issue of cost coverage was irrelevant to the Postal Service pricing in this case. (OCA//USPS-T1-23, DFC/USPS-T1-17.) Yet, not only does the PRA require a reasonable assignment of institutional costs, Commission precedent also demands a reasonable assignment. The Postal Service has not demonstrated that the high cost coverages are reasonable, and, arguably, the Postal Service has even treated them as irrelevant. (See DBP/USPS-43, DBP/USPS-50: "Marking up production costs was not pursued for the following reasons.")

5. The Pricing Factors in §3622 of the PRA Are Not Met.

Witness Yeh discusses the value (§3622(b)(2)) of the service actually provided. (Yeh at 8-11.) The witness refers to the convenience of including stationery with the stamped envelope. The utilitarian stamped envelope offers some of the convenience offered by the Premium Stamped stationery. It includes a stamp with the envelope.

Yet, even where there is the added convenience of the utilitarian stamped envelope, the Commission recently recommended a very low cost coverage of 104.1 percent. The Postal Service wants to increase the cost coverage by many times that amount, merely for the added convenience of including stationery with the stamped envelope.

The only other justification the Postal Service offers for this higher cost coverage is the artistic value of the printing on the paper. OCA suggests that the added artistic imagery and the special printing, as attractive as it may be, does not justify such a large increase in the cost coverage. The cost of the production of the stationery and the printing of the artistic image are accounted for in the production costs which are then marked up.

Moreover, in one aspect, the convenience value of the Premium Stamped Stationery product may be lower than that provided by the utilitarian stamped envelope product because the premium stamped stationery product must be first folded to produce an envelope, whereas the utilitarian stamped envelope is purchased as a completely enclosed finished envelope product. When sealed, the utilitarian envelope is entirely closed whereas the Premium Stamped Stationery product is not sealed on two sides.

Witness Yeh's testimony also fails to offer any specific support for her conclusion that the proposed revenue in excess of costs "represents a reasonable contribution toward covering the institutional costs of the Postal Service" as required by factor (b)(3). (§3622(b)(3).) (Yeh at 9.) The witness's conclusion lacks support and is offered without reference to other cost coverages and so is contrary to the Commission's precedent of establishing prices on the basis of measured cost coverages.

Witness Yeh also considers the effect of the proposed rate upon the general public (§3622(b)(4)), concluding that the fee will not adversely affect the general public or private delivery enterprise, only those who buy the product. She says the proposed fee is comparable to similar stationery products. It is apparent that the Postal Service's prices are justified solely on the basis of a small survey of similar products in the market with some similarity to the quality of the Premium Stamped Stationery, without any regard for the cost of the product. Those customers who purchase the product at the proposed pricing level will be adversely affected because they will be asked to pay a premium far in excess of the cost of this monopoly product.

Finally, although witness Yeh contends the products offer aesthetic value to customers (Yeh at 7, 8, and 10), the witness admits the fees do not explicitly reflect, and thus do not further, the pricing factors in §3622(b)(8) concerning the educational, cultural, scientific, and informational value to the mailer.

Therefore, the Postal Service's proposed price range, not being within normal levels of cost coverage, are based on the tenuous arguments that mailers do not have to buy this product if they do not want to, the price is similar to a few other comparable sheets of stationery in the market, that the contribution of institutional costs is, without explanation, reasonable, and lastly that the images on the product are aesthetic, although they are not deemed to be educational, cultural, scientific or informational in value.

The case simply has not been made to justify the cost coverages at either the maximum price in the proposed range or even at the current price. Finally, even the minimum price of two times the First-Class letter rate produces excessive and

unreasonable cost coverages. At a fee of \$0.82, two times the First-Class letter rate, the average cost coverage of both issues would be 283 percent ($\$0.82/\0.29). For the Disney Friendship Stamped Stationery alone, its cost coverage would be 372 percent ($\$0.82/\0.22). Even for the Garden Bouquet Stamped Stationery alone, the cost coverage would be 228 percent. It is apparent the Postal Service's benchmark of a multiple of the First-Class letter rate is misplaced.

6. The Value of the Premium Stamped Stationery Does Not Warrant A High Cost Coverage

At best, the Postal Service is contending that the high value of the product (the premium provided to the mailer by offering "quality paper stock," and the convenience of including an unfolded stamped envelope designed as a letter sheet for purchase in one transaction) are sufficient to justify a high cost coverage. Neither the witness, nor the responses of the Postal Service to interrogatories, justify their conclusion.

Nevertheless, several points are pertinent in response to the contention. The cost coverage for utilitarian stamped envelopes is only 104.1 percent. Yet, in one sense, utilitarian envelopes offer a greater value to the mailer than a Premium Stamped Stationery. The utilitarian envelope is already assembled and ready for mailing and encloses the message on all sides, offering considerably more privacy and is not as flimsy as the envelope that is created by sealing a Premium Stamped Stationery envelope which is not sealed on all four sides. In any event, the value of the convenience of the pre-folded utilitarian envelope rather than an unfolded sheet of stamped paper ready for sealing may be a factor reducing the value of the PSS product compared to the utilitarian envelope. That is a further reason for reducing, or at least

offsetting, the higher value the Postal Service attributes to the convenience of stationery being designed as part of the envelope.

Unlike the stamped utilitarian envelope, the PSS is designed for a message, yet the amount of paper in the utilitarian envelope compared to the stationery letter sheet is not significantly different. The fact that the premium stationery envelope is engineered for a message and includes a sheet of paper to write a message does not provide very much additional convenience. The Postal Service witness looked to commercial sheets of stationery as a comparison of value and found that the cost of commercial sheets of stationery, although they are not stamped, provide a basis for the range of prices suggested. The approach to pricing ignores the time honored look to the cost of the product. Nothing here suggests that the product has so much value as to justify pricing it at the level of a commercially available sheet of stationery. That is simply not the appropriate way to approach pricing under the PRA.

Since 1947, the Postal Service has sold letter sheets for international mail at the face value of the postage imprinted on the sheet. (DBP/USPS-29.) In 1972, the Postal Service also sold five Surface and Air Mail postal cards with images on the back. (DBP/USPS-28.) Those products with images provided aesthetic value, yet in those cases the Postal Service did not increase the rate above the face value of the stamp. (Ibid.) The Postal Service has not distinguished those products from the current products.

Moreover, the Postal Service has disavowed any special philatelic value to these Premium products. (DBP/USPS-33-34, DBP/USPS-30.) According to the Postal Service, that is not a value to be taken into consideration when establishing the range of

rates. The only special value is apparently the value the Postal Service places on the quality stock paper and the artistic image to be considered when determining the retail selling price within the established range.

There is one other problem with the proposed pricing. The range of prices permits the Postal Service to charge whatever it chooses within that range. The product here has been characterized as being on quality paper stock. The proposed DMM language in §963.1 does not define the product as having quality paper stock to distinguish it from other potential products of lesser quality.¹⁶ Thus, although these two Premium Stamped Stationery products do obviously have a thicker paper than the thin letter sheets sold in the past, the Postal Service has not demonstrated that the higher quality paper stock is more expensive to purchase than the thin paper letter sheets. More importantly, there is no guarantee that the Postal Service will not revert to using the thin letter sheets in its next Premium Stamped Stationery issue, which it could under the language proposed for the DMM. The DMM should specify that the stationery must be of a quality comparable to the paper in the current issues. If the Postal Service decides to use significantly different paper stock with significantly different costs, the classification may need to be revised or another class created.

The record demonstrates that the implicit cost coverage of the Premium Stamped Stationery at current prices falls outside a reasonable level; and the selling price of the stationery must be reduced. The minimum cost coverage may be drawn from the cost coverage recommended for the utilitarian stamped envelope. Given the aesthetic value of the product, the maximum cost coverage should be not greater than the highest cost

¹⁶ Proposed DMM §963.1 states, "Premium Stamped Stationery is decorated stationery with First-Class Mail postage imprinted or impressed on it, and offered for sale by the Postal Service." (Request, Attachment A, at 1.)

coverage recommended in the last rate case, 211.8 percent. Based on the average cost of the two Premium Stamped Stationery issues, the Commission should recommend fees of from \$0.302 to \$0.613, developed from the above range of cost coverages. To avoid unnecessary expense, the price should not be reduced until current stocks are sold or destroyed.¹⁷

B. Premium Stamped Cards

The Postal Service proposes a Premium Stamped Card classification in Fee Schedule 964 with a pre-printed stamp and an image that decorates the entire reverse side. Proposed DMM §964.1 says, “Premium Stamped Cards are postal cards with First-Class Mail postage imprinted or impressed on them, decorated on the reverse side, and offered for sale by the Postal Service.”

The Postal Service proposes a rate range, excluding postage, of from one to three times the standard card rate, or \$0.26 to \$0.78. Currently the Postal Service is selling several different cards for the same unit prices. (See DBP/USPS-21.) Following implementation of the new card rate of 26 cents, the proposed price range for the PSC, excluding postage, would be from \$0.52 to \$0.78 per card. Currently, the Postal Service is selling several cards: Art of Disney Celebration, Disney Romance, Disney Friendship and Baseball Sluggers at stamp fulfillment centers plus five additional issues on sale at local post offices, all with the same packaging for the price of \$9.75 for twenty

¹⁷ When sold in multiples, in a package (or individually), the product should not be sold at fractions of less than one cent. But see OCA/USPS-T1-16 where the Postal Service notes this is not precluded by the proposed fee schedules.

stamped cards. (DBP/USPS-20-21, 24.)¹⁸ Excluding postage of 26 cents per card, the selling price per card is \$0.2575 per card. (OCA/USPS-T1-10.)¹⁹

The approximated unit cost of the Art of Disney, Romance Premium Stamped Card is \$0.14. (Yeh at 5, OCA/USPS-T1-22.) The effective cost coverage at the maximum proposed rate of three times the new card rate of \$0.26 would be 557 percent. (Ibid.) At the minimum proposed rate of one times the card rate, the implicit cost coverage would be 186 percent ($\$0.26/\0.14). At the current selling price of \$9.75, or \$0.2575 per card, the implicit cost coverage, again excluding postage, is 184 percent. (Ibid.)²⁰

To calculate price points for the premium cards, witness Yeh studied a sample of postcards at their full retail price. (OCA/USPS-T1.) The sample is suspect. Of the five cards included in the sample, four of them would not qualify for the card rate because their length exceeds 6 inches. (DBP/USPS-37.) The calculated average retail price of the cards of \$0.498 is therefore not a sound figure to rely upon to establish price points. Even though the price of the one card in the sample that qualified for the card rate (\$0.831) is higher than the average of all the cards in the sample, the study is flawed and does not provide sufficient evidence of comparable market prices justifying the range of fees proposed of from \$0.26 to \$0.78. The absence of credible evidence about

¹⁸ Also on sale, and an exception to the usual packaging, is the larger Florida Wetlands card sold at the First-Class letter rate. The recommended cost coverage implicit in the card fees should also apply to this card.

¹⁹ The Postal Service is selling cards at \$9.95 for 20 cards with 24 cents preprinted postage and other cards at \$9.75 for 20 cards with 23 cents preprinted postage. Thus, each card is selling for the same unit price, excluding postage, of 25.75 cents.

²⁰ The current selling price is virtually identical to the proposed minimum price of one times the card rate. If the maximum in the range was two times the \$0.26 card rate, the cost coverage at that level would be (52/14) or 371 percent, an extraordinarily high cost coverage.

the market price of cards comparable to the Premium Stamped Card compels reference to the production costs of the cards plus a reasonable markup to establish the range for their fee.

OCA opposes the proposed maximum price range for the card for the same reasons stated above with respect to the postal stationery. Also, in the case of cards, the Postal Service proposes a range up to three times the standard card rate whereas the cards have been priced for several years at less than 2 times the stamped card rate. (DBP/USPS-25.) The Postal Service says it needs the wide range to accommodate other higher quality or special editions. (Ibid.) The requested range is not only out of line with current pricing, but it assumes even higher quality products may be offered. Yet, the Postal Service has not demonstrated why even higher quality products should not have a different fee classification; otherwise, the Postal Service will be able to increase the prices on the current products without incurring the costs that justify the higher price for the entire class.

The proposed maximum cost coverage is inconsistent with Commission practice and the Postal Service has not justified that change. Although the Premium Postal Card does have an aesthetic artistic value and a higher quality of paper, the Premium Postal Card, in all pertinent respects, provides the same service as the utilitarian stamped card, if not less. A utilitarian stamped card, unlike the utilitarian envelope, includes an area for writing a message. In the case of the utilitarian card, the message area is on the side opposite the pre-stamped side. With the utilitarian card, there is also the possibility of including some message on the stamped side. On the other hand, the printed image on the Premium Stamped Card covers one entire side of the card in the

manner of a commercial picture postcard. The area for writing the message is limited to one-half the stamped side. On the Premium cards there is also a brief printed statement in the upper left-hand corner of the stamped side related to the image on the card, further restricting the space for a message. Thus, less than one-fourth of the Premium Stamped Card has message space whereas the utilitarian stamped card provides at least one-half, and perhaps a little more, of its area for a message.

Unlike the stamped stationery, the Premium Stamped Card does not require folding to prepare for mailing. In that respect, it is identical to the utilitarian stamped card. Thus, the only differences between the utilitarian stamped card and the Premium Stamped Card are the quality of paper, the image on the front of the cards, and, on the utilitarian card, a greater portion of the card may be used for a message.

Just as with the Premium Stamped Stationery, the Postal Service admits that cost coverage was not relevant to it when determining its recommended price range. Moreover, the Postal Service contends cost coverage should not be relevant to the price of the Premium Stamped Card classification. Rather, the Postal Service argues that the aesthetic image and paper quality justify a price premium. However, the quality of the paper is reflected in the printing costs-part of the production cost of the product.

(OCA/USPS-T1-14.)

Although the Postal Service plans to continue using quality stock paper for these products (OCA/USPS-T1-14.), it did not include “quality stock paper” in the definition of these products in order to “accommodate unanticipated changes.” The range of fees permits resetting the price to accommodate such changes. (Ibid.) On the downside, the range of fees would allow the Postal Service to substantially lower the paper quality and

still ask premium prices for the card products. (See DBP/USPS-55.) This is another reason why the price range should be tied to the attributable costs of the products rather than to the unrelated First-Class card rate benchmark.

The utilitarian stamped cards received a cost coverage of 135.2 percent in the last rate case based on the selling price of \$0.02. (PRC Op. at 464.) The cost of the Disney card, including proxies for retail window service is \$0.14. (OCA/USPS-T1-22.) The significantly higher production costs thus take into account the premium paper quality and special image on the Disney card.

The Postal Service has not justified a cost coverage that is so different from the Commission's practice. OCA therefore proposes a rate range based upon the range of reasonable cost coverages—from a minimum fee with an implicit cost coverage set at the level of the utilitarian stamped card and, recognizing the aesthetic value and paper quality in the Premium Stamped Card, a maximum fee based on a cost coverage equal to the highest coverage allowed by the Commission in the last rate case. OCA, therefore, supports a fee range with a cost coverage between that allowed for stamped cards of 135.2 percent and the highest cost coverage permitted in Docket No. R2006-1 of 211.6 percent. On the basis of the \$0.14 card cost, excluding postage, the Postal Service would have a range of pricing possibilities for the Art of Disney Celebration Premium Stamped Card and other Premium Stamped Cards of \$0.189 per unit up to \$0.296 per unit. The current selling price for the Premium Stamped Cards of \$0.2575 falls within this range.²¹

²¹ When sold in multiples, in a package (or individually), the product should not be sold at fractions of less than one cent.

CONCLUSION

For the above reasons, the Commission should recommend approval of the proposed permanent classifications for the Premium Stamped Stationery and Premium Stamped Card classes. Reference to the quality paper currently used should be included in the DMM definitions for those classes.

In the case of the Premium Stamped Stationery, based on the average cost of the two Premium Stamped Stationery issues, and a range of implicit cost coverages of from 104.1 percent to 211.6 percent, the Commission should recommend fees of from \$0.302 per unit to \$0.613 per unit.

In the case of the Premium Stamped Card classification, based on the cost of the Art of Disney Romance issue, and a range of implicit cost coverages from 134.2 percent to 211.6 percent, the Commission should recommend a range of fees for Premium Stamped Cards of \$0.189 per unit to \$0.296 per unit.

Respectfully submitted,

Shelley S. Dreifuss
Director
Office of the Consumer Advocate

Kenneth E. Richardson
Attorney

901 New York Ave. NW Suite 200
Washington, D.C. 20268-0001
(202) 789-6830; Fax (202) 789-6891